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# Mackay & Knobel Enterprises, Inc., A Utah Corporation v. Teton Van Gas, Inc., A Corporation, Van Gas, A Corporation : Respondent's Brief

Utah Supreme Court

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IN THE SUPREME COURT  
OF THE  
STATE OF UTAH

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MACKAY & KNOBEL ENTER-  
PRISES, INC., a Utah Corpora-  
tion,

*Plaintiff and Appellant,*

vs.

TETON VAN GAS, INC., a Cor-  
poration, VAN GAS, a Corpora-  
tion,

*Defendants and Respondent.*

Case No.  
11,555

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RESPONDENT'S BRIEF

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Appeal from judgment of the Third Judicial  
District Court for Salt Lake County.  
Honorable Merrill C. Faux, Judge

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FILED

JUN 28 1961

Clerk

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*Defendants and Respondent.*

Case No.  
11,555

---

RESPONDENT'S BRIEF

---

NATURE OF THE CASE

Plaintiff-Appellant sought by its complaint to recover for fire damages sustained when a gas line broke on plaintiff's property.

DISPOSITION IN LOWER COURT

The District Court granted defendant's motion dismiss plaintiff's complaint for the reason that the plaintiff corporation lacked sufficient corporate existence to prosecute the action because its corporate charter had been suspended.

## RELIEF SOUGHT ON APPEAL

Respondent seeks to have this Court affirm the trial court's action.

## STATEMENT OF FACTS

The original complaint in this action was filed in the Third Judicial District Court in and for Salt Lake County, May 29, 1964 (R.20). The action there filed was for all practical purposes identical to the one filed in this case (R.22-25). That action was dismissed for the reason that the plaintiff's corporate powers had been suspended on October 14, 1963 (R. 26).

A substantially identical suit was later filed in the District Court of Summit County in March 1967 (R.1-4), after the plaintiff corporation had been reinstated in October of 1966 (R.26). However, the corporate powers of plaintiff were again suspended on September 30, 1967 (R. 26), for its failure to pay its franchise taxes. Because of the 1967 suspension, defendant moved the court for a dismissal of plaintiff's action because the plaintiff lacked the necessary legal standing to sue (R.18, 19), the same basis upon which the earlier action was dismissed by the District Court of Salt Lake County (R.20,21). The District Court of Summit County granted defendant's motion and dismissed plaintiff's complaint (R. 36).

## ARGUMENT

POINT I. THE POWERS WHICH ARE GRANTED TO A CORPORATION ARE WITHDRAWN WHEN THE SECRETARY OF STATE SUSPENDS A CORPORATE CHARTER FOR FAILURE TO PAY ITS FRANCHISE TAXES.

The corporation is a creature of the state. The corporate entity could not exist before the enactment of legislation which permitted the creation of a corporation. The corporation must necessarily rely entirely upon powers and limitations, conferred and imposed by the State. The Utah Business Corporation Act contained in Title 16 of the Utah Code, enumerates the powers of a corporation. Section 16-10-4 (b), Utah Code Annotated (1953) provides:

“Each corporation shall have power: . . .

(b) to sue and be sued, complain and defend in its corporate name.”

One of the obligations of a Utah corporation is to pay taxes. Section 59-13-61 Utah Code Annotated (1953) imposes a limitation if such taxes are not paid:

“If a tax computed and levied hereunder is not paid before 5 o'clock p.m. on the last day of the eleventh month after the date of delinquency, *the corporate powers, rights and privileges of the delinquent taxpayer, if it is a domestic corporation, shall be suspended,* (emphasis added) and if a foreign corporation, it shall thereupon forfeit its rights to do intrastate business in this state.”

“The tax commission shall transmit the name of each such corporation to the secre-

tary of state, who shall immediately record the same in such manner that it may be available to the public. The suspension or forfeiture herein provided for shall become effective from the time such record is made, and the certificate of the secretary of state shall be prima-facie evidence of such suspension or forfeiture."

As noted from the above quoted statute, a domestic corporation's failure to pay its taxes may result in the suspension of its "corporate powers, rights and privileges." The corporate powers which are suspended are necessarily the powers which had been bestowed by the legislature as enumerated by the Utah Business Corporation Act, Title 16, Utah Code Annotated (1953). As stated above, one of those powers is the power to sue. Therefore, when the corporate powers are suspended under 59-13-61 Utah Code Annotated (1953), as was done in the case at bar, one of the powers suspended is the power to sue. Once the corporation's powers are suspended, the corporation becomes civilly dead. While its form may exist, the life and power of the company is withdrawn.

A. UTAH STATUTES PROVIDE APPROPRIATE PROCEDURES FOR THE SUSPENDED CORPORATION TO REGAIN ITS POWERS AND RIGHTS:

The statutes have also provided appropriate procedures for a suspended corporation to regain its rights and powers. A corporation whose charter has been suspended may be reinstated upon payment of



delinquent taxes owed to the State. Section 59-13-63, Utah Code Annotated (1953) provides:

“Revivor or Reinstatement.

“(1) Any corporation which has suffered the suspension or forfeiture referred to in the preceding section may be relieved therefrom upon making application therefor, in writing, and paying the tax and the interest and penalties for nonpayment of which the suspension or forfeiture occurred . . . ”

If, however, the corporation continues in its failure or refusal to pay its taxes, its powers remain suspended, an appropriate penalty for the corporation's failure to comply with a pre-requisite for continued existence within the state. If a reinstatement is not entered, the state may completely eliminate the delinquent corporate structure by involuntary dissolution. Section 16-10-89 (a) Utah Code Annotated (1953), states:

“A corporation may be dissolved involuntarily by a decree of the district court in an action filed by the attorney general when it is established that:

“(a) The corporation has failed to file its annual report within the time required by this act, or its corporate powers, rights and privileges have been suspended as provided by section 59-13-61, Utah Code A n n o t a t e d (1953) ;”

Once a dissolution proceeding is initiated by the state some of the corporate powers are restored. Accordingly, during dissolution proceedings for the purpose

of winding-up its affairs, a corporation may sue. Section 16-10-100 and 101. However, once the company's business is wound-up, the corporation ceases to exist.

It appears from a study of the statutes that the legislature has provided that a corporation:

—may continue to exist if it complies with the statutes.

—shall have only those powers as set out in the statutes.

—shall be obligated to pay specified taxes to the state.

—upon failure to pay prescribed taxes, its corporate powers and rights will be withdrawn until payment is made.

—upon continued failure to pay taxes may be wholly dissolved by the state.

—during the process of dissolution is permitted limited powers to conclude its business and to wind up its affairs.

B. CRIMINAL SANCTIONS AGAINST PERSONS WHO ATTEMPT TO EXERCISE CORPORATE POWERS DURING SUSPENSION EMPHASIZES THE INTENDED COMPLETE PROHIBITION AGAINST THE EXERCISE OF SUCH POWERS WHILE THE CORPORATION IS UNDER SUSPENSION.

The legislature's refusal to allow the exercise of corporate powers once the corporation fails to pay its taxes is further emphasized by Section 59-13-62,

Utah Code Annotated (1953), which attaches a criminal penalty to the "... exercise of any of the rights, privileges or powers of any such domestic corporation ..." while the same is under suspension. Under this section any person "... who attempts or purports to exercise any of the rights, privileges or powers ..." of a corporation under suspension is guilty of a misdemeanor. This plain language is unequivocal and is a direct expression of intent that even the apparent corporate powers are not to be utilized following state suspension.

POINT II. A SUSPENDED CORPORATION MAY NOT VOLUNTARILY EXERCISE POWERS WITHDRAWN BY THE STATE UNDER THE GUISE OF WINDING UP ITS AFFAIRS.

Although the appellant has argued that a corporation should be allowed to wind up its affairs after its corporate charter has been suspended, it has not produced any evidence that the present suit is in furtherance of that purpose. Even so, the right to exercise suspended corporate powers can only be exercised for this purpose under the supervision of the state, during dissolution proceedings under Section 16-10-89, Utah Code Annotated (1953).

At the time the court ruled on defendant's motion to dismiss, plaintiff's charter was under suspension. The corporate powers had been withdrawn by the State, and acts in furtherance of winding up its affairs could only be exercised under its supervision.

A. SECTION 59-13-61, U.C.A., 1953 HAS NOT BEEN CONSTRUED BY THIS COURT TO PERMIT A CORPORATION TO SUE FOLLOWING SUSPENSION OF ITS CORPORATE POWERS.

Appellant suggests that a suspended corporation should be permitted to "wind up" and refers to what he terms a "long line of Utah cases." Contrary to Appellant's assertion, this court has never had before it a case involving the right of a domestic corporation to sue after its powers have been suspended under Section 59-13-61, Utah Code Annotated (1953).

Appellant relies on several cases where corporate charters were *forfeited* under earlier statutes. However, the cases cited do not involve a statute similar to the one presently under consideration. Section 59-13-61 Utah Code Annotated (1953), provides for both suspension and *forfeiture* of corporate charter and powers. Suspension applies to domestic corporations and forfeiture applies only to foreign corporations, because this state does not have power to dissolve a corporation of another state. It can only restrict its right to do business here.

None of the cases cited on pages 3 and 4 of Appellant's Brief, involves the *suspension* of a domestic corporation's powers for its failure to pay its franchise taxes. In fact, all but one of the Utah cases cited there were decided before the enactment of Section 59-13-61, U.C.A., 1953, which provides for the suspension of corporated powers for nonpayment of taxes.

Only one of the appellant's "long line of cases" was decided after the enactment of Section 59-13-61, Utah Code Annotated (1953). This case is *Warren v. Dixon Ranch Co.*, 23 Utah 416, P.2d 741 (1953). Although the decision post dates the statutes, the case does not involve a suit filed by a corporation after suspension of its charter. Rather, the case is a quiet title action in which the defendant company was made a party after suspension in 1934. The reason for the suspension does not appear in the decision. One of the company's directors, who was also a trustee, was served with process in 1951, both individually and as a company official. Because of his failure to answer the complaint, or to notify other stockholders so that they might file an answer, a default judgment was entered. The company's motion to set aside the default was denied.

The case simply holds that service of process on a director of a suspended corporation is sufficient to acquire jurisdiction over the corporation. This case is of little assistance here.

#### B. CORPORATE RIGHTS UNDER DISSOLUTION.

The rights of a corporation upon dissolution are set forth in Sections 16-10-100 and 101, U.C.A., (193), which provide that such a corporation may enforce its rights or claims which existed prior to dissolution. An action may be prosecuted by the dissolved corporation, and its corporate existence continues for the purpose of winding up its affairs. In

this connection the corporation may sue and be sued. Provision for payment of all taxes and debts of the corporation is provided in the proceeding. Upon this basis some limited rights are thus permitted to be exercised by the dissolved corporation.

However, a discussion about dissolution is immaterial here because the appellant corporation was never dissolved.

#### C. EXTRAORDINARY WRITS MAY BE GRANTED AGAINST A SUSPENDED CORPORATION.

Appellant relies upon Rule 65 B(b) (1) Utah Rules of Civil Procedure for authority that a suspended corporation is authorized to prosecute a law suit. This Rule authorizes an appropriate action against a corporation whose charter has been forfeited. This provision, rather than supporting appellant's position, argues heavily against it because a procedure is specifically provided authorizing a civil action to prevent such prohibited activity. Relief is provided when " . . . any corporation has offended against any provision of the law, . . . or has committed an act amounting to a surrender or a forfeiture of its corporate rights, privileges and franchises . . . " This is consistent with respondent's position that a suspended corporation has no powers to act.

#### D. IF A SUSPENDED CORPORATION WERE PERMITTED TO SUE AND OTHERWISE DO BUSINESS TO WIND-

UP ITS AFFAIRS IT COULD AVOID THE PAYMENT OF TAXES.

A corporation may properly wind up its affairs by following the procedure for voluntary dissolution, which provides for the payment of taxes and debts. In the absence of a voluntary proceeding the State may proceed with an involuntary dissolution proceeding which also makes provision for payment of delinquent taxes and debts. Undoubtedly the legislature withdrew all the corporate powers from a suspended corporation from winding up its affairs, dispersing the funds so accumulated for purposes other than payment of taxes and debts and leaving the state and creditors to look where they might for satisfaction of their claims.

If the appellant wishes to wind-up its affairs it must do so by following the required procedure. It should not be permitted to leave taxes unpaid, ignore the statutes and pursue its own course without regard to the rights of the sovereignty which gave it life.

Appellant cites cases where other states have held that a failure to pay corporation taxes does not prevent the corporation from suing. However, those cases do not involve an interpretation of the statutes contained in the Utah law, nor the public policy expressed therein, and are not helpful precedent in this case.

E. THE PRIOR UTAH STATUTE AUTHORIZING A CORPORATION, WHOSE CHARTER HAD BEEN FORFEIT-



ED, TO WIND UP ITS AFFAIRS HAS BEEN REPEALED.

Utah's Business Corporation Act, Section 16-10-143, U.C.A., (1953), deals with the effect of the repeal of the prior act. The recent corporation act enacted a new code dealing with corporations and repealed all prior laws. Section 16-10-143 U.C.A. (1953), provides that the repeal did not affect rights established under the prior law.

Whether or not plaintiff may have been able to have maintained the present suit under the provisions of the old statute, Section 16-1-2, U.C.A., (1953), repealed by Chapter 28, Laws of Utah, 1961, is moot. The fact is that the plaintiff corporation must look to the present law for its rights and privileges because it can only exist and exercise those powers granted to it by statute. The right to sue, if such there were, under the prior statute, was withdrawn by an express repeal of the statute upon which appellant relies, and new provisions were adopted dealing with suspended powers. To argue that appellant may have had certain rights under the prior law which could not be abridged by the new act, is to deny to the legislature its right to regulate corporations which are the product of its own power. Certainly the legislature cannot and did not intend to impair established contract rights. But that question is not involved in this action.

Even so, under the prior statute plaintiff could not have successfully maintained the present suit.



Section 16-1-2 U.C.A., (1953), to which Appellant refers and which was repealed, stated:

“Any corporation organized under the laws of the territory or state of Utah whose franchise has heretofore expired or may hereafter expire by limitation or by forfeiture, or by, dissolution by decree of court may nevertheless continue for the purpose of winding up its affairs; and to effect this purpose may sell or otherwise dispose of real and personal property, sue and be sued, contract, and exercise all other incidental and necessary powers.”

This statute permitted corporations to exercise powers in order to wind up their affairs in the nature of a voluntary or involuntary dissolution.

F. THE PRINCIPAL PROVISIONS OF REPEALED SECTION 16-1-2, U.C.A., (1953), WERE ENACTED INTO THE PRESENT LAW.

The principal provisions of repealed Section 16-1-2, U.C.A., (1953), have been re-enacted in the Utah Business Corporation Act, 16-10-100 and 16-10-101, U.C.A., (1953). Neither the prior provision nor the present statute permits a lawsuit to be instituted by a corporation whose charter has been *suspended because of its failure to pay its taxes.*

The legislators when considering the adoption of the Model Business Corporation Act were probably aware of the problem now facing the court. The tax suspension statute 59-13-61 U.C.A., (1953) was enacted in 1931 and the legislature was fully

aware of its provisions, when the Business Corporation Act of 1961 was adopted. Section 16-10-89, U.C.A., (1953), dealing with involuntary dissolution of a corporation whose powers, rights and privileges had been suspended under Section 59-13-61, U.C.A., (1953), was enacted to permit the state to dissolve the corporation, if necessary, to obtain payment of taxes and to protect the rights of creditors and stockholders. The legislature thereby not only recognized the problem existing in connection with a suspended corporation, but also provided a procedure by which the state through the corporation, could effectively prosecute claims on behalf of the corporation. Without such a procedure a suspended corporation which could not, or would not pay taxes due, would remain in suspension. Thus, the suspended corporation may be involuntarily dissolved by court decree initiated by the Attorney General. Had the legislature allowed a suspended corporation to continue to exercise its powers contrary to the tax suspension provision, it would have entirely eliminated the effect of any penalty imposed under Section 59-13-61, U.C.A., (1953). The appellant whose charter was in suspension should not be permitted to avoid the provisions of this statute by merely claiming to have been engaged in winding up its affairs. To sanction such conduct would permit a corporation to avoid the payment of taxes to the state.

POINT III. ALTHOUGH A CORPORATION MAY SUE FOLLOWING A COURT ORDERED DISSOLUTION, SUCH IS NOT A SOUND REASON TO PERMIT A SUSPENDED CORPORATION TO SUE.

Appellant has suggested that since a corporation involuntarily dissolved has limited rights to sue, that the legislature did not intend to impose a more severe penalty upon a corporation whose charter has been suspended. However, the legislature has stated that a domestic corporation which does not pay its taxes declared to be due, is deprived of its corporate powers until they are paid. If such a corporation were permitted to exercise its corporate powers there would be no other effective penalty for preventing tax delinquencies. If the tax delinquency continues the state may find it advisable to involuntarily dissolve the corporation under the supervision of the court, and require payment of taxes due from its assets and distribute the remaining assets to creditors and stockholders. The entire plan as established by the legislature is not only reasonable, but is necessary.

Public policy favors equal application of the law. If respondent corporation is required to pay its taxes in order to maintain its rights and powers to sue and defend, then the appellant corporation should be required to do likewise. Public policy favors the orderly winding up of suspended corporations, which protects the state, creditors and stockholders. To permit the appellant corporation to maintain a lawsuit during suspension under the guise of wind-

ing up its affairs would provide a convenient procedure by which corporate obligations can be avoided. Public policy not only favors but requires payment of taxes. The legislature expressed its intention clearly in Section 59-13-61 U.C.A., (1953). The statute makes no mention of merely prohibiting a delinquent domestic corporation from engaging in new business as suggested by plaintiff. The legislature simply stated that:

“ . . . the corporate powers, rights and privileges of the delinquent taxpayer, if it is a domestic corporation, shall be suspended, . . . ” 59-13-61, U.C.A., (1953).

Whether or not plaintiff is entitled to commence a new action is not now before the court. The only question before the court is whether the district court has properly dismissed plaintiff's lawsuit. Respondent respectfully contends that the trial court acted in accordance with law.

## CONCLUSION

Plaintiff's action was originally commenced in May, 1964. Because plaintiff corporation failed to pay its taxes its charter was suspended October 14, 1963. For this reason the plaintiff's lawsuit was dismissed on defendant's motion. After plaintiff corporation paid the required taxes, it filed another action in another county in March 1967. Because another annual tax was unpaid the plaintiff's powers were again suspended September 30, 1967. Defend-

ant made a motion that the action be dismissed because of plaintiff's incapacity to maintain the action. The motion was granted and the complaint was dismissed.

The Utah statutes concerning the power of a domestic corporation are comprehensive and clear:

- when in good standing it is granted power to sue. Section 16-10-4 (b) Utah Code Annotated, (1953).
- it must pay specified taxes, which if not paid will result in the suspension of the corporate charter and powers. Section 59-13-61 Utah Code Annotated, (1953).
- to regain its full powers the corporation must pay the tax due. Section 59-13-63 Utah Code Annotated, (1953).
- failure to pay delinquent taxes may result in an involuntary dissolution proceeding, during which a limited right to sue for the purpose of winding up its affairs under court supervision, is granted. Sections 16-10-89, 16-10-100, and 16-10-101 Utah Code Annotated (1953).

A suspended corporation loses the right to function as a corporation. It may not assume to exercise the power to prosecute an action under the guise of winding up its affairs, and thus defeat the purposes of the statute designed to require payment of delinquent taxes, debts and rights of stockholders.

The judgment of dismissal should be affirmed.

Respectfully submitted,

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